



<b>Title</b>	<b>Ho Tung Gardens Saga and the Basis of Compensation under the Antiquities and Monuments Ordinance: A Comparative and Incentive Case Study on Regulatory Takings</b>
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# HO TUNG GARDENS SAGA AND THE BASIS OF COMPENSATION UNDER THE ANTIQUITIES AND MONUMENTS ORDINANCE: A COMPARATIVE AND INCENTIVE CASE STUDY ON REGULATORY TAKINGS



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*Regulatory schemes that mandate historical preservation for private property are increasingly common. This article employs the attempt to preserve Ho Tung Gardens as a case study to examine problems in the design of compensation measures for such schemes. The compensation provision of Antiquities and Monuments Ordinance (Cap 53) is ambiguously worded, and this article argues that this Ordinance provides compensation only for the additional costs associated with the maintenance of historical buildings and does not compensate owners for property value depreciation. However, this article also argues from an incentive perspective that adequate compensation should be provided to property owners for such depreciation to ensure that the government and the public duly account for the true costs of heritage conservation. In addition, adequate compensation eliminates the perverse incentives for owners to preemptively demolish historical buildings in order to avoid the regulatory regime. This article draws on similar legislative experiences in the UK to propose guidelines for reforming the compensation provision.*

## I. Introduction

The topic of heritage conservation has frequently been controversial. At the root of the controversy lies the tension between preserving historical buildings, on the one hand, and embracing economic development, on

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the other.<sup>1</sup> This tension is particularly acute when private entities own the historical buildings. Owing to increased public awareness about the importance of heritage conservation, jurisdictions around the globe have enacted legislative schemes to mandate the preservation of privately owned historical buildings.<sup>2</sup> Such legislation pits the public interest in heritage conservation against the rights of private property owners to develop the property. Aggravating matters is the absence of adequate compensation for economic losses suffered by private owners as a result of development restrictions. Because of the substantial diminution of property value, imposing legal restrictions on private property is properly conceived of as a form of regulatory takings.<sup>3</sup> However, neither the provision nor the adequacy of compensation is typically mandated by the constitutional protection of property against government takings.<sup>4</sup> This has resulted in a wide array of compensation measures among the different legal regimes – if any are provided at all.

This article utilises the attempted preservation of Ho Tung Gardens – an important historical mansion located in a prime residential area in Hong Kong<sup>5</sup> – to examine the pitfalls in the design of compensation regimes for historical preservation. Under Antiquities and Monuments Ordinance (Cap 53) (the “Ordinance”),<sup>6</sup> the government has the power to declare a historical building a monument and prohibit all development that is incompatible with heritage conservation.<sup>7</sup> Compensation for private owners is provided for, although vaguely described as what the court “thinks [is] reasonable in the circumstances”.<sup>8</sup> The Ho Tung Gardens saga began in 2010 when the owner, in a typical attempt to realise the economic potential of the site, applied for a building permit to demolish the mansion and to construct new residential buildings worth HK\$3 billion (US\$ 380 million).<sup>9</sup> Despite the widely acknowledged

<sup>1</sup> Matthew Brown and Richard L Stroup, “Markets Versus Takings and Regulation: Deciding the Future of the Past” in Bruce L Benson (ed), *Property Rights: Eminent Domain and Regulatory Takings Re-Examined* (Palgrave Macmillan, 2010) 211, 211–212; Michael Ross, *Planning and the Heritage: Policy and Procedures* (E & FN Spon, 2nd ed, 1996) 1–9.

<sup>2</sup> For a survey on the various legal regimes of historical conservation, see generally Consuelo Olimpia Sanz Salla, *The Protection of Historic Properties: A Comparative Study of Administrative Policies* (Wit Press, 2009).

<sup>3</sup> For a detailed exposition of the conceptual and legal issues relating to regulatory takings, see generally Steven J Eagle, *Regulatory Takings* (Lexis Nexis, 3rd ed, 2005).

<sup>4</sup> Stephen L Kass, Judith M LaBelee and David A Hansell, *Rehabilitating Older and Historic Buildings* (John Wiley & Sons, 2nd ed, 1993) 209–219.

<sup>5</sup> See below Part II.B.1.

<sup>6</sup> Antiquities and Monuments Ordinance (Cap 53).

<sup>7</sup> *Ibid.*, ss 3 and 6. See below Part II.A.

<sup>8</sup> *Ibid.*, s 9(2). See below Part III.

<sup>9</sup> Joyce Ng, “Ho Tung Mansion Saved from Demolition”, *South China Morning Post* (HK), 26 January 2011, p 1.

historical significance of Ho Tung Gardens,<sup>10</sup> the government ultimately did not declare the site a monument because of the potential hefty compensation payable to the owner under the Ordinance.<sup>11</sup>

This article makes three arguments in relation to the Ho Tung Gardens saga. The first is a relatively narrow legal argument that the assumption of hefty compensation that dominated both the public debate and the government calculus is not grounded in valid legal principles. A careful examination of the text of the Ordinance, the relevant legislative debate and the background case law on regulatory takings indicates that the compensation payable under the Ordinance is simply the additional costs associated with maintaining the historical buildings, as opposed to the commonly held assumption that the depreciation in land value and/or the loss of redevelopment value would be payable to owners of property under the Ordinance.

The second argument is a broader normative argument from the incentive perspective that the assumption of significant compensation, although not legally required under the Ordinance, is a normatively desirable benchmark. Compensation for the depreciation in land value and/or loss of redevelopment facilitates a more accurate assessment of the true costs of heritage conservation. In turn, this promotes a more informed public discourse about whether the historical preservation of a particular site is indeed socially desirable. Moreover, it helps avoid the perverse incentives for owners of old buildings to pre-emptively demolish or alter the buildings in order to avoid the financially damaging restrictions that are the consequence of being declared a monument.

In addition, the incentive perspective reveals the illogical distinction drawn in the Ordinance between in-kind compensation and monetary compensation. Only compensation paid out in cash is subject to the mandatory legislative oversight of budgetary control, while there are limited checks on how the executive branch utilises in-kind compensation (eg land exchange and beneficial land use regulatory actions) to compensate the affected owners.<sup>12</sup> However, both in-kind and monetary compensation are economically valuable to the recipients and economically costly to the providers. The public at large suffers both when the in-kind compensation paid out can be monetised to a larger quantum than the legally required amount, and when the exercise of regulatory powers is driven by

<sup>10</sup> Joyce Man and Joyce Ng, "Keep Historic Estate Intact, Adviser Urges", *South China Morning Post* (HK), 11 October 2011, p 3; Joyce Ng, "Gardens a Living Reminder of our Colonial Past, Says Historians" *South China Morning Post* (HK), 26 January 2011, p 1; Olga Wong and Joyce Ng, "Public to Grade 1,400 Sites", *South China Morning Post* (HK), 20 March 2009, p 1.

<sup>11</sup> See below Part II.B.3.

<sup>12</sup> See below Part IV.C.

compensation requirements rather than by the original policy objectives of the regulatory scheme. Nevertheless, the case study of Hong Kong confirms that the perverse incentive created by this disparity in legal treatment of the in-kind and monetary compensation does induce the executive branch to rely excessively on the former while being unduly averse towards the latter.

Reform is thus necessary. Together with a comparative analysis of the UK legal regime, this article outlines a set of guidelines to reform the compensation provision under the Ordinance and similar legislation. In particular, compensation must be adequate. The depreciation of property value utilised in the UK legal regime is a viable benchmark. However, any reform should avoid the current UK legal position that excludes from compensation the reduction in land value caused by other regulatory schemes, even if the regulatory burdens are advanced for the purposes of heritage conservation.<sup>13</sup> In addition, the compensation scheme should avoid distinguishing between in-kind compensation and monetary compensation.

This article is organised into six parts. Part II sets out the basic framework of the Ordinance and the case study of the Ho Tung Gardens saga. Part III critically examines the basis of compensation under the Ordinance and concludes that the commonly held assumptions during the Ho Tung Gardens saga that the Ordinance mandated hefty compensation were legally incorrect. Part IV utilises an incentive perspective to highlight the merits of adequate compensation on both the government decision-making process and on the incentives of private property owners to preserve historical buildings. Part V draws on the UK experience to propose reform of the compensation provision under the Ordinance and similar legislation. Part VI concludes the article.

## II. The Ho Tung Gardens Saga

### A. Basic Legal Framework in Hong Kong

The Ordinance was enacted in 1971 (and has been effective since 1976) when Hong Kong was a British colony.<sup>14</sup> Considered long overdue,<sup>15</sup> the Ordinance was the first legislation specifically dedicated to protecting local heritage. Under the Ordinance, the Secretary for Development (hereinafter, the “Secretary”) is authorised and responsible for preserving

<sup>13</sup> See below Part V.A.2.

<sup>14</sup> For an account of the political and legal history of Hong Kong, see Johannes Chan, “From Colony to Special Administrative Region” in Johannes Chan and CL Lim (eds), *Law of the Hong Kong Constitution* (Sweet & Maxwell, 2011) 3, 5–12.

<sup>15</sup> Official Reports of Proceedings (Legislative Council of Hong Kong), 3 November 1971, 180, 182.

objects of historical, archaeological and paleontological interest.<sup>16</sup> The Secretary is advised by the Antiquities Advisory Board, which is established under s 17 of the Ordinance and consists of individuals appointed by the Chief Executive.<sup>17</sup> The approval of the Chief Executive is necessary for significant decisions, such as paying private entities under the Ordinance.<sup>18</sup>

The main thrust of the Ordinance is the power to declare that certain premises are monuments.<sup>19</sup> Once declared a monument, no demolition, alteration or other construction work can be undertaken on the premises without a permit from the Secretary.<sup>20</sup> A provisional power to declare the premise a proposed monument was added in 1982 to provide for interim restraints on development until a decision on the status of the premises is finalised.<sup>21</sup> Declaring a site a proposed monument has a maximum validity period of 12 months and cannot be extended with respect to privately owned sites.<sup>22</sup>

The safeguards against these potential far-reaching restrictions on private property are primarily twofold. First, the Ordinance provides avenues for objections by the owner or lawful occupier of the affected property.<sup>23</sup> However, this is only an internal administrative appeal that ends with the Chief Executive in Council.<sup>24</sup> Although judicial review of the Chief Executive's decision is not precluded, the review would be limited to whether the decision has been made in accordance with the relevant legislative provisions and other common law principles that ensure that the process was procedurally and substantively fair.<sup>25</sup>

<sup>16</sup> Antiquities and Monuments Ordinance (Cap 53) s 2. For a discussion of the administrative structure, see David Lung, "Built Heritage in Transition: A Critique of Hong Kong's Conservation Movement and the Antiquities and Monuments Ordinance" (2012) 42 *Hong Kong Law Journal* 121, 124–125; Gordon N Cruden, *Land Compensation and Valuation Law in Hong Kong* (LexisNexis, 3rd ed, 2009) 38.

<sup>17</sup> Cruden (n 16 above), p 38. Under Hong Kong current political institution arrangement, the Chief Executive is the head of government, akin to the Governor of Hong Kong under British colonial rule: see Benny Tai, "The Chief Executive" in Chan and Lim (n 14 above), p 181 (discussing the appointment and powers of the Chief Executive).

<sup>18</sup> For example, Antiquities and Monuments Ordinance (Cap 53) s 11(4).

<sup>19</sup> *Ibid.*, s 3. For general discussion, see Cruden, (n 16 above), pp 38–40.

<sup>20</sup> *Ibid.*, s 6.

<sup>21</sup> *Ibid.*, s 2A. The approval of the Chief Executive is necessary before the Secretary can make a declaration of monument, but is not required for the provisional power of declaration of proposed monument.

<sup>22</sup> *Ibid.*, s 2B.

<sup>23</sup> *Ibid.*, ss 2C and 4.

<sup>24</sup> *Ibid.*, ss 2C(6) and 4(6). The Chief Executive in Council, or Executive Council, is an advisory body to the Chief Executive under the Basic Law and arguably serves the role of a cabinet in a British parliamentary system: see Richard Cullen, Xiaonan Yang and Christine Loh, "Executive Government" in Chan and Lim (n 14 above), pp 249, 257–258.

<sup>25</sup> See *Chu Hoi Dick v Secretary of Home Affairs* (unrep., HCAL 87/2007, [2007] HKEC 1471) (CFI) (dismissing the challenge against the administrative decision under the Ordinance of not declaring Queen's Pier a monument).

Second, the Ordinance provides for a right of compensation for the “financial loss” caused by the refusal to grant a construction permit.<sup>26</sup> The amount of the compensation should be either agreed upon by the Secretary and the owner of the affected property<sup>27</sup> or assessed by the District Court as to what “it thinks reasonable in the circumstances”.<sup>28</sup> As is immediately apparent from the wording of the statutory provisions, little guidance is provided with respect to the compensation. The ambiguity as to what is “reasonable in the circumstances” is highlighted in the recent Ho Tung Gardens saga discussed in the next section.

## **B. The Attempted Preservation of Ho Tung Gardens**

### *1. Historical significance*

The historical significance of Ho Tung Gardens reflects an important, if unsavoury, aspect of the colonial history of Hong Kong. The Peak, a prime residential area on Hong Kong Island, was governed by exclusionary zoning that prohibited non-Europeans from residing there.<sup>29</sup> Ho Tung Gardens was the first and only exception to the racial zoning, when the Eurasian Ho Tung was granted permission to build a Chinese-style garden (and accompanying mansion) on the Peak in 1927 in appreciation for mediating a strike that spread through Guangzhou and Hong Kong.<sup>30</sup> The site covers 120,000 square feet and incorporates a Chinese renaissance architectural style.<sup>31</sup> There is general consensus among conservation experts on the important historical value of Ho Tung Gardens.<sup>32</sup> The premises was classified as a Grade I historic site in 2009,<sup>33</sup> which is the highest grade given and reflects the “outstanding merit” of the premises.<sup>34</sup> Grading is based on expert assessment of the following six criteria: historic

<sup>26</sup> *Ibid.*, s 8.

<sup>27</sup> *Ibid.*, s 8(2)(a).

<sup>28</sup> *Ibid.*, s 9(2).

<sup>29</sup> Gillis Heller and Daphne SW Wong, ‘The History of Exclusionary Zoning Laws in Hong Kong’ (2010) 40 *Hong Kong Law Journal* 609, 614–618.

<sup>30</sup> Ng (n 10 above).

<sup>31</sup> *Ibid.*

<sup>32</sup> Man and Ng (n 10 above); Ng (n 10 above). There are some commentators who are sceptical of the premise’s heritage significance, although none proclaimed any particular expertise on the matter: Albert Cheng, “Due Process”, *South China Morning Post* (HK), 17 March 2012, p 15; Jake van Der Kamp, “Let’s Face it: the Ho Tung Garden’s House has no Merit”, *South China Morning Post* (HK), 30 October 2011, p 16.

<sup>33</sup> Wong and Ng (n 10 above).

<sup>34</sup> There are three grades under the scheme: Grade I are given to buildings of outstanding merit for which every effort should be made to preserve; Grade II are for buildings of special merit for which efforts should selectively be made to preserve; Grade III are for buildings of some merit but not yet qualified for consideration as possible monuments: see Lung (n 16 above), pp 126–127; Cruden, (n 16 above), pp 38–39.



value, architectural value, social value, rarity, authenticity and group value.<sup>35</sup> The grading system is independent of the Ordinance and has no legal effect; it merely serves as an internal guideline for conservation efforts.<sup>36</sup>

## *2. Declaration of proposed monument*

The saga officially began at the end of 2010, when grand-daughter of Ho Tung and owner of the premises, applied for a building permit to demolish the mansion and build 11 blocks of four-storey houses on the site.<sup>37</sup> Restricted to evaluating the plan's structural safety issues, the Building Department issued an approval in December 2010 but alerted heritage officials.<sup>38</sup> The development plan would yield 60,000 square feet of residential floor area and was estimated to be worth HK\$3 billion at the then-market price of approximately HK\$50,000 per square foot.<sup>39</sup>

Government officials attempted to negotiate with the owner about the preservation issues, including incentives and assistance in maintenance but indicated that they were rebuffed.<sup>40</sup> The application and approval of the building permit prompted the Secretary to declare Ho Tung Gardens a proposed monument on 28 January 2011. This temporarily halted the demolition of the mansion and bought time for continued negotiations.<sup>41</sup>

## *3. The negotiation process*

During the negotiation process, both parties advanced different offers after the proposed monument declaration. The owner offered to preserve the Chinese garden but knock down the mansion, although this was rejected because expert advisers to the Antiquities Advisory Board indicated that conservation required the preservation of the entire estate.<sup>42</sup> The Secretary offered a land swap of a site adjacent to the premises, which was zoned as a green belt and was reputed to have similar vistas and land values as the Ho Tung Gardens.<sup>43</sup> The land swap was rejected by the owner, who wrote to the press stressing that her decision was not motivated by profit but by

<sup>35</sup> Wong and Ng (n 10 above).

<sup>36</sup> Lung (n 16 above), pp 126–127; Cruden (n 16 above), pp 38–39.

<sup>37</sup> Ng (n 9 above). Ms Ho objected to the grade-one historic rating in 2009 on grounds that Ho Tung did not live there for long, there was no important family events held there, and the building's interior had been considerably altered: Ng (n 10 above).

<sup>38</sup> Ng (n 9 above).

<sup>39</sup> *Ibid.*

<sup>40</sup> *Ibid.*

<sup>41</sup> Joyce Ng, "Ho Tung Gardens Owners Told of Listing", *South China Morning Post*, 29 January 2011, p 3.

<sup>42</sup> Man and Ng (n 10 above).

<sup>43</sup> Joyce Ng, "Land Swap Offers to Save Historic Peak Villa", *South China Morning Post*, 22 October 2011, p 1.



her desire to continue to live on the site as a homeowner by replacing the mansion with 10 “tasteful cottages”.<sup>44</sup>

After the one-year deadline lapsed, the government made a last-ditch offer that permitted the original 5,800 square meters of residential space to be developed but required the preservation of the façade of the main building, but this was rejected.<sup>45</sup> Both parties decided to wait until a new Chief Executive was in power because the outgoing Chief Executive Donald Tsang was disinclined to make a decision.<sup>46</sup> In December 2012, the new administration announced that it had given up plans to save the site.<sup>47</sup> The Secretary explained that the decision was financial in nature because the government was reluctant to spend billions in public funds on private heritage sites.<sup>48</sup>

#### 4. *The unresolved question of compensation*

The Ho Tung Gardens saga is notable for the assumptions that were commonly made regarding the compensation in the public discourse. The Secretary and lawmakers all noted that there was uncertainty regarding the compensation level the court will award.<sup>49</sup> The chairman of the Antiquities Advisory Board, Bernard Chan, opined that it might be good for this case to go to court to set a precedential benchmark about the price of conservation.<sup>50</sup> However, the figure of HK\$3 billion (the estimated value of the redevelopment plans) was often referred to as the likely amount of compensation that would have been awarded.<sup>51</sup> Letters in the press frequently mentioned the same HK\$3 billion figure as the price tag to preserve Ho Tung Gardens,<sup>52</sup> and this perception was also reflected by lawmakers.<sup>53</sup> The various offers made to the owner by the Secretary were similarly based on the assumption that a hefty compensation would be payable for the loss in redevelopment potential.

<sup>44</sup> Joyce Ng, “Ho Tung Villa Owner Fights Back”, *South China Morning Post*, 26 October 2011, p 3.

<sup>45</sup> Joyce Ng, “Proposal to Save Mansion Rejected”, *South China Morning Post*, 8 March 2012, p 1.

<sup>46</sup> Joyce Ng, “Tsang Still Undecided on Peak Garden Plan”, *South China Morning Post*, 14 June 2012, p 3.

<sup>47</sup> Joyce Ng and Olga Wong, “Heritage Policy Failure as Peak Mansion to Go”, *South China Morning Post*, 5 December 2012, p 1.

<sup>48</sup> Joyce Ng and Olga Wong, “Double U-turn as Ho Tung Plan is Abandoned”, *South China Morning Post*, 5 December 2012, p 1.

<sup>49</sup> Joyce Ng, “Taxpayers Face HK\$3b Bill for Mansion”, *South China Morning Post*, 25 October 2011, p 1.

<sup>50</sup> Ng (n 42 above).

<sup>51</sup> Ng and Wong (n 47 above); Man and Ng (n 10 above).

<sup>52</sup> “Letters”, *South China Morning Post*, 3 November 2011, p 16 (Lila Ho: “However, one problem is that preserving the house could cost taxpayers HK\$3 billion”; Mark Peaker: “HK\$3 billion could be used to build a new children’s hospital, or better care facilities for the elderly”).

<sup>53</sup> Ng (n 42 above).

There were dissenting views about the basis of compensation that should arise from a declaration of monument. During the negotiations after the lapse of the one-year proposed monument declaration, a consultancy report commissioned by Heritage Hong Kong Foundation, a private non-profit organisation, argued that the compensation should be the net present value of the forgone rental value of the 10 cottages, estimated at approximately HK\$200 million.<sup>54</sup> William Meacham, a former board member of the Antiquities Advisory Board, went even further in arguing that the compensation provision under the Ordinance is limited to financial losses caused by governmental actions in inspecting, repairing and excavating the site.<sup>55</sup>

### III. The Legal Basis of Compensation

What then is the proper legal basis for compensation under the Ordinance arising from a monument declaration? This part resolves this unfortunately unanswered issue by critically examining the statutory wordings, legislative background and relevant case laws on regulatory takings.

#### A. Statutory Wordings

Compensation arising from the declaration of the monument is set forth in ss 8 and 9 of the Ordinance.

##### *Section 8: Compensation*

- (1) Subject to this section, the Authority may, with the prior approval of the Chief Executive, pay to the owner or lawful occupier of a proposed monument or monument compensation in respect of financial loss suffered or likely to be suffered by him by reason of (Amended 59 of 2000 s 3):
  - (a) the exercise by the Authority, or by a designated person authorized by him, of the powers specified in s 5(1); or
  - (b) a refusal to grant a permit or any conditions imposed in a permit.

<sup>54</sup> Joyce Ng, "Bid to Break Heritage Deadlock", *South China Morning Post*, 12 March 2012, p 1.

<sup>55</sup> Joyce Ng, "Potential Peak Mansion Lifeline Rejected by Board", *South China Morning Post*, 18 December 2011, p 4.

- (2) The compensation shall be such amount as may be:
  - (a) agreed between the Authority and the owner or lawful occupier of the proposed monument or monument; or
  - (b) assessed by the District Court under s 9.
- (3) No compensation shall be awarded under this section in respect of financial loss that has been or may be suffered in connection with a contract made or anything done by the owner or lawful occupier of the proposed monument or monument after the service of a notice under s 2A(4) or 4(2).

*Section 9: Assessment of Compensation by District Court*

- (1) In default of agreement under s 8(2)(a), the owner or lawful occupier may apply to the District Court to assess the amount of compensation payable under s 8.
- (2) The District Court may, on such application, award to the applicant such compensation as it thinks reasonable in the circumstances.

The deficiencies and ambiguities in the wording are immediately apparent. There is no expressly provided benchmark for compensation in the event that the government and property owner cannot agree on the quantum of compensation. Assessment by the District Court<sup>56</sup> under s 9 merely provides for “such compensation as it [the District Court] thinks reasonable in the circumstances”. The sole tangible guidance is from s 8(1), which states that the compensation is “in respect of financial loss suffered or likely to be suffered by him [owner or lawful occupier] by reason of” either the s 5(1) provision (provision of power of entry and repair) or “a refusal to grant a permit or any conditions imposed in a permit”.<sup>57</sup>

This lack of specificity contrasts starkly with compensation provisions set forth in other Hong Kong ordinances that involve infringement of private interests in land. The most obvious example is the statute for compulsory acquisition of land, with ss 10–12 of the Lands Resumption Ordinance (Cap 124)<sup>58</sup> setting out in detail the assessment method for the

<sup>56</sup> The District Court usually involves a District judge sitting alone, but the judge may allow not more than two assessors to sit with him on a purely advisory basis: Cruden (n 16 above), p 42.

<sup>57</sup> This is pursuant to the power under s 6(1) that stipulates a permit by the Authority is needed before any construction work can be undertaken on the declared (or proposed) monument.

<sup>58</sup> Lands Resumption Ordinance (Cap 124).

damages payable. Similarly, the Mass Transit Railway (Land Resumption and Related Provisions) Ordinance (Cap 276)<sup>59</sup> has an entire attached schedule to specify the basis on which compensation is to be assessed for each of the various losses that may be claimed.

Significantly, this contrast in specificity between the ordinances is not the result of timing. The Mass Transit Railway (Land Resumption and Related Provisions) Ordinance was enacted in 1974, contemporaneous with the Ordinance that was enacted in 1971 and implemented in 1976. Although the Land Resumption Ordinance has been in force since the late nineteenth century, the detailed provisions on compensation were added in 1974.<sup>60</sup> Nor can the difference be explained by the regulatory taking nature of the Ordinance. The Mass Transit Railway (Land Resumption and Related Provisions) Ordinance expressly allows claims of loss that arise from the refusal or withdrawal of permits by the Building Authority, with the basis of compensation set as the reduction of the market value of the land as a result of the refusal or withdrawal.<sup>61</sup>

Indeed, the absence of compensation guidance in the Ordinance is best highlighted by comparison with the contemporaneous Country Parks Ordinance (Cap 208).<sup>62</sup> The Country and Parks Ordinance was enacted in 1976 to designate and manage country parks in Hong Kong. It shares a legislative framework that resembles the Ordinance. As with the effect of monument declaration under the Ordinance, s 10 of the Country and Parks Ordinance provides that no new development may be undertaken on a site in the area without approval after the premises is designated as part of a country park.<sup>63</sup> Compensation is set forth in a specific provision for losses arising out of the refusal to grant approvals for development.<sup>64</sup> However, unlike the Ordinance, the specific basis of compensation assessment is clearly demarcated. In particular, the reduction of land value resulting from the refusal to grant development approval is explicitly claimable<sup>65</sup> under parameters set forth in the calculation of land value.<sup>66</sup>

<sup>59</sup> Mass Transit Railway (Land Resumption and Related Provisions) Ordinance (Cap 276) Sch I (Part I).

<sup>60</sup> Cruden (n 16 above), pp 13–14.

<sup>61</sup> Mass Transit Railway (Land Resumption and Related Provisions) Ordinance (Cap 276) ss 10 and 11, Sch I (Part I), (n 59 above) (expenses and fees accrued pursuant to an approved plan are also claimable upon withdrawal).

<sup>62</sup> Country Parks Ordinance (Cap 208).

<sup>63</sup> *Ibid.*, s 10. See Cruden, (n 16 above), pp 227–230.

<sup>64</sup> *Ibid.*, s 19.

<sup>65</sup> *Ibid.*, s 19(2).

<sup>66</sup> For example, land value should be assessed in accordance with the Lands Resumption Ordinance: s 19(4), while no account shall be taken of any increase or decrease in the value of land that is attributable to the country park designation: Country Parks Ordinance (Cap 208)s 19(3).

## B. Legislative History

The conspicuous ambiguity in the compensation provision of the Ordinance is not a legislative oversight. The issue of compensation was actually raised in the Ordinance's legislative debate. In response to criticism from a lawmaker (Mr Cheung) about the possible arbitrariness that might flow from the determination of compensation by the Authority rather than an independent tribunal,<sup>67</sup> then-Secretary of Home Affairs (DCC Luddington) explained that "such compensation would not be in regard to any expropriation of land".<sup>68</sup> Rather, the "compensation payable under this clause of the bill would be in relation to, for instance, the requirement to retain a building or portion of a building in its existing condition and not to demolish it".<sup>69</sup> He also observed that such assessment had not been attempted before in Hong Kong and "will have to be the subject of some experiment".<sup>70</sup>

It is notable that there was no apparent reference to parallel UK provisions during the legislative debate.<sup>71</sup> Indeed, expressly disavowing expropriation is significant in light of UK compensation provisions that expressly provide the basis of compensation to include, among other factors, the diminution of property value arising from the monument declaration.<sup>72</sup> Such specific and relatively generous grounds for compensation were provided largely because the reference point for compensation under UK legislation has been, since its earliest manifestation, compulsory acquisition.<sup>73</sup>

The criticism by Mr Cheung resulted in modification of the structure of the compensation provisions. The original scheme envisioned that the amount of compensation would be determined by the Authority with a right of appeal to the District Court.<sup>74</sup> This was amended into the current form that provides for initial negotiation between the Authority and the land owner.<sup>75</sup>

<sup>67</sup> Official Reports of Proceedings (Legislative Council of Hong Kong.), 17 November 1971, 218.

<sup>68</sup> *Ibid.*, p 220.

<sup>69</sup> *Ibid.*

<sup>70</sup> *Ibid.*

<sup>71</sup> While the UK Ancient Monuments and Archaeological Areas Act was only enacted in 1979, it was mainly a consolidation of existing laws that include the Historic Buildings and Ancient Monuments Act of 1953 (Ch 49). Section 12 of this Historic Buildings and Ancient Monuments Act of 1953 provided for compensation to persons whose interests in the declared monument is "injuriously affected" by the declaration or "suffers damages" because of refusal to grant approval for construction works. For a discussion of the legislative evolution, see Simon Halfin, "The Legal Protection of Cultural Property in Britain: Past, Present and Future" (1995) 6 *DePaul-LCA J. Art & Ent. L.* 1, 3–13.

<sup>72</sup> See below Part V.A.

<sup>73</sup> Joseph L. Sax, "Is Anyone Minding Stonehenge? The Origins of Cultural Property Protection in England" (1990) 78 *Cal. L. Rev.* 1543, 1547 and 1565; Halfin (n 71 above), pp 3–7.

<sup>74</sup> Official Reports of Proceedings (Legislative Council of Hong Kong), 3 November 1971, 183.

<sup>75</sup> Official Reports of Proceedings (Legislative Council of Hong Kong), 1 December 1971, 256–257.

### C. Case Law on Regulatory Takings

The restrictions on redevelopment accompanying monument declaration are essentially a form of regulatory takings – ie diminishing private property interests through government regulations. In the case of Ho Tung Gardens, a monument declaration would have deprived the owner of the substantial sales revenue from the ten luxury cottages to be built on the demolished site. As opposed to compensation that is widely expected whenever property interests are acquired by the state outright, compensation for regulatory takings is much more controversial.

The issue was clarified in Hong Kong by the seminal case of *Fine Tower Associates Ltd v Town Planning Board*.<sup>76</sup> The case arose from a challenge to property protection under Art 105 of the Basic Law (Hong Kong's de facto constitution). The Court of Appeal defined the legal test of regulatory takings as whether there is "de facto deprivation" in which there is "the removal of any meaningful use, of all economically viable use".<sup>77</sup> This approach represents the court's survey of the UK/European approach of "de facto deprivation" in *Sporrong and Lönnroth v Sweden* and *Grape Bay Ltd v A-G of Bermuda* in addition to the US regulatory takings jurisprudence from *Lucas v South Carolina Coastal Council* and *Penn Central Transportation Co v City of New York*.<sup>78</sup> The court noted the relevance of "investment-back expectations" as a factor to consider<sup>79</sup> and observed that in Hong Kong, "[i]t is an incident of ownership that the uses permitted by the authorities may change. Land is purchased with that knowledge, actual or imputed".<sup>80</sup> Applying the test, the court dismissed the claim by the property owner, finding that the reduction of height restrictions from 85 meters to 35 meters and the imposition of the new 44 per cent open space requirement continued to allow for considerable development and does not approximate an unconstitutional deprivation of property.<sup>81</sup>

The regulatory takings principle enunciated in *Fine Tower Associates Ltd v Town Planning Board* has been applied subsequently in two reported Hong Kong cases. Both cases involve only lower trial courts, but the application to the facts is illustrative. The first case, *Man Yee Transport Bus Co Ltd v Transport Tribunal*,<sup>82</sup> involved the cancellation of the passenger service license and vehicle license of a bus as sanctions for providing

<sup>76</sup> [2008] 1 HKLRD 553 (CA). For a discussion of the case and the relevant principles, see Michael Wilkinson, "Land" in Chan and Lim (n 14 above), pp 359, 392–394.

<sup>77</sup> *Fine Tower Associates Ltd v Town Planning Board* (n 76 above), p 564.

<sup>78</sup> *Ibid.*, pp 560–564.

<sup>79</sup> *Ibid.*, pp 562–563.

<sup>80</sup> *Ibid.*, pp 567.

<sup>81</sup> *Ibid.*, pp 565–569.

<sup>82</sup> (unrep., HCAL 122/2008, [2008] HKEC 1775) (CFI).

unauthorised bus services. The court rejected the challenge based on Art 105 and observed that, although revocation of the licenses prevented the bus owner from using the vehicle on the roads in Hong Kong, the bus could be sold for good value in the second-hand market or could be used outside Hong Kong.<sup>83</sup> The second case, *Oriental Generation Ltd v Town Planning Board*,<sup>84</sup> involved zoning restrictions imposed by the Town Planning Board. The court affirmed the principles on regulatory takings set out in *Fine Tower Associates Ltd v Town Planning Board* in obiter<sup>85</sup> after quashing the restrictions on the basis of arbitrariness.<sup>86</sup> It is notable that the court recognised the validity of the Town Planning Board's authority to take nearby historical sites into account in drawing up zoning maps.<sup>87</sup>

#### ***D. Summary: Loss in Redevelopment Value Not Compensable***

Gordon N Cruden, former president of the Hong Kong Land Tribunal, opined in his academic work that “general principles of compensation would apply” to the Ordinance, with the courts seeking to “ascertain the extent to which the market value of the land had been diminished as a consequence of the [monument declaration]”.<sup>88</sup> This is despite Cruden's acknowledgement that the District Court “is given a wide discretion to assess compensation” under s 9(2).<sup>89</sup> Indeed, his references to other ordinances in which compensation is payable for diminution in value<sup>90</sup> does not support his intuition because those ordinances authorising compensation for diminution in value typically have express wordings setting out that particular basis of compensation.<sup>91</sup>

Indeed, the failure to mention compensation for diminution of land values in the vague wording of the Ordinance arguably reflects a legislative intention that does not envision such compensation. As observed in the legislative debate, the provision of compensation was primarily based on costs associated with maintaining historical buildings in their original state. This reflects the logical concern in historical conservation that

<sup>83</sup> *Ibid.*, [13]–[15] (CFI). For a critical discussion of this case, see Oliver Jones, “Right to Property” in Chan and Lim (n 14 above), pp 913, 924–925.

<sup>84</sup> [2012] 3 HKC 369 (CFI).

<sup>85</sup> *Ibid.*, [89]–[90].

<sup>86</sup> *Ibid.*, [61]–[82].

<sup>87</sup> *Ibid.*, [7] (they include one grade 1 listed building and one grade 3 listed building).

<sup>88</sup> Cruden (n 16 above), p 42.

<sup>89</sup> *Ibid.*

<sup>90</sup> *Ibid.*

<sup>91</sup> See Mass Transit Railway (Land Resumption and Related Provisions) Ordinance (Cap 276), Country Parks Ordinance (Cap 208) and Lands Resumption Ordinance (Cap 124), discussed in above Part III.A.



extra expenses are unavoidable in preserving buildings in their original state.<sup>92</sup> However, this departs from the framework of UK provisions that are premised on the compulsorily government acquisition of land. This is also unlike the other two contemporaneous pieces of legislation, the Mass Transit Railway (Land Resumption and Related Provisions) Ordinance and the Country Parks Ordinance, which expressly contemplate compensation based on reductions in land values caused by development restrictions.

Importantly, the provisions of compensation for loss in market value arising from the refusal of the Building Authority to grant permits for development was specifically inserted into the Mass Transit Railway (Land Resumption and Related Provisions) Ordinance only after the issue was raised during the legislative debate of the second and third readings.<sup>93</sup> Indeed, the Attorney General proposing the bill emphasised that the compensation amendment is “solely in the context of the mass transit railway” and stated that “[i]t must not be assumed that the Government’s agreement to change in this respect is setting a precedent for the future in relation to other public works or projects for the benefit of the community as a whole”.<sup>94</sup>

In addition, the compensation for the Ordinance must be interpreted in light of the regulatory takings baseline established under *Fine Towers Association*. The monument declaration under the Ordinance is unlikely to result in “the removal of any meaningful use, of all economically viable use”. Section 5(3) of the Ordinance provides that the owner and parties authorised by the owner could not be excluded from any part of the monuments, ie the owner remains free to utilise the premise in its existing state. More importantly, monument declaration does not preclude all development. Development plans that do not involve demolition or substantial alterations to the historical structure are not likely to be refused, as evidenced by the proposals advanced by the Secretary during the negotiations over Ho Tung Gardens. Monument declaration under

<sup>92</sup> Charles Mynors, *Listed Buildings and Conservation Areas* (Pearson, 2nd ed, 1995) 121.

<sup>93</sup> Official Reports of Proceedings (Legislative Council of Hong Kong), 17 July 1974, 1027; Official Reports of Proceedings (Legislative Council of Hong Kong), 14 August 1974, 1180.

<sup>94</sup> Official Reports of Proceedings (Legislative Council of Hong Kong), 14 August 1974, 1161. While the Attorney General also stated that this issue of compensation would be reflected in the substantial review of the Town Planning Ordinance: *id.*, it is telling that no form of compensation was ultimately provided in the Town Planning Ordinance (Cap 131) itself. The issue of compensation did not generate any debate during the enactment of the Country Parks Ordinance (Cap 208), but the reason is probably that the detailed and relatively generous compensation provisions have already been in place in the bill at the first reading: see Official Reports of Proceedings (Legislative Council of Hong Kong), 7 January 1976, 382–386; Official Reports of Proceedings (Legislative Council of Hong Kong), 10 March 1976, 637–648.

the Ordinance is not a *prima facie* unconstitutional infringement of private property and does not require compensation.

Thus, this article submits that assuming that the Ordinance contemplates considerable compensation for the loss of development rights is legally incorrect. The express wording and legislative intent of the Ordinance indicates a compensation basis and an approach to assessment that is distinct from the conventional reduction in land value envisioned in contemporaneous and similar legislation. Given the high threshold of regulatory burdens necessary to invoke compensation under the existing regulatory takings doctrine in Hong Kong, the District Court will be on solid legal ground in awarding compensation under the Ordinance primarily based on additional out-of-pocket maintenance and repair costs required by mandate to preserve the property.

In any event, it is notable that the hefty compensation figure assumed in the Ho Tung Gardens saga is erroneous because of simple arithmetic. Even if the compensation should be calculated by the diminution of property value caused by the monument declaration, the fact that the redevelopment can generate HK\$3 billion in sale revenue by no means implies that the compensation should be set as HK\$3 billion. In addition to deducting the costs necessary for development, the compensation amount must be further reduced by the value of the existing property.<sup>95</sup> The latter fact is not trivial because it would have remained a luxury mansion in a prime location. Moreover, although the restrictions on development inherent in a monument declaration would result in a decrease in property value, it did not prohibit all development. The loss arising from the refusal to allow the HK\$3 billion redevelopment must be mitigated by the possibility of alternative developments that would be approved.

#### IV. An Incentive Perspective in Regulatory Takings

The absence of a legal basis for substantial compensation under the Ordinance does not necessarily discount the merits of such compensation. This part argues that paying significant compensation under the Ordinance, although not a legal requirement thereunder, is a normatively desirable benchmark from an incentive perspective.

<sup>95</sup> In *Hui Sui Sam v Director of Public Works* (unrep., MT Ref 3/82) involving compensation for the MTR line, the value of the development permitted under the imposed restrictions and the additional construction costs necessary to facilitate the original development were deducted from the value of the original development: Cruden (n 16 above), p 396.

An incentive perspective of the law examines the incentives created by a given legal regime on the relevant actors to analyse whether the relevant actors would engage in a socially desirable course of action. Although the incentive perspective assumes that the relevant actors are rational, the incentive calculus should not be restricted to those of a monetary nature.<sup>96</sup> In the realm of public law, in which the government is a major player in the formulation and implementation of policies, the incentive perspective is particularly valuable because it examines the pressures and inducements that shape government actions.

### A. Constraints on Government Actors

The exercise of regulatory powers is an inherent function of the government, particularly in the current regulatory state.<sup>97</sup> The exercise of regulatory powers is subject to the basic expectations and requirements that it should only be exercised to promote the general social welfare. This expectation and requirement thus became an important justification for the denial of compensation to private individuals who suffered losses under the regulatory regime.<sup>98</sup> Except in the narrowly defined categories of unconstitutional regulatory takings,<sup>99</sup> costs imposed by regulations are the expected and legitimate burdens that should be borne by private entities for the general benefit of society.

Conversely, the incentive perspective treats government officials as it treats other private individuals. Government officials are affected by their own self-interest and other factors that render them unable to actively and single-mindedly pursue the public interest during the performance of regulatory functions.<sup>100</sup> This scepticism towards the political process gives rise to fairness arguments to justify compensation for regulatory takings. Injustice may occur when a lack of compensation for affected private individuals means

<sup>96</sup> Stephen J Spurr, *Economic Foundations of Law* (Routledge, 2nd ed, 2010) 2–4 (“For cost is a very broad idea in economics: depending on the situation, the cost of a given action may include money, time, emotional stress, discomfort, the risk of physical injury or criminal prosecution, or other undesirable consequences”).

<sup>97</sup> David J Barron and Todd D Rakoff, “In Defense of Big Waiver” (2013) 113 *Colum. L. Rev.* 265, 266–267.

<sup>98</sup> Mildred E Warner, “Regulatory Takings and Free Trade Agreements: Implications for Planners” (2009) 41 *Urb. Law.* 427, 428; Christopher Serkin, “The Meaning of Value: Assessing Just Compensation for Regulatory Takings” (2005) 99 *Nw. U. L. Rev.* 677, 713–714; James Audley McLaughlin, “Majoritarian Theft in the Regulatory State: What’s A Takings Clause For?” (1995) 19 *Wm. & Mary Envtl. L. & Pol’y Rev.* 161, 190–192.

<sup>99</sup> See Above Part III.C.

<sup>100</sup> Paul Niemann and Perry Shapiro, “Compensation for Taking When Both Equity and Efficiency Matter” in Benson (n 1 above), p 55; John A Rogovin and Rodger D Citron, “Lessons from the Nextwave Saga: The Federal Communications Commission, the Courts and the Use of Market Forms to Perform Public Functions” (2005) 57 *Admin. L. Rev.* 687, 695.

that they are required to bear the entire cost of the regulatory actions.<sup>101</sup> In particular, there is concern that the powers of the government will be abused to the detriment of vulnerable minorities.<sup>102</sup> The common constitutional requirement of compensation for physical takings (eminent domain) reflects such counter-majoritarian protection of minorities.<sup>103</sup>

Another strain of argument from this incentive perspective addresses the efficiency of government actions. While taking a less negative view of the political process, this argument focuses on the risks of the government making socially inefficient decisions when it is not required to take into account the costs of those decisions. The constraints of information costs impede even a politically responsive government in allocating resources effectively for the public interest.<sup>104</sup> Within the context of regulatory takings, providing compensation serves as an important constraint on government by compelling it to confront the costs and benefits of government actions.<sup>105</sup> Undercompensation (or worse, no compensation) may result in inefficient government actions because the full social costs of the government actions are not internalised.<sup>106</sup> The government will be induced to impose excessive regulatory burdens instead of engaging socially cheaper alternatives that may cost the government more.<sup>107</sup>

Both arguments resonate in the Ho Tung Gardens saga. Although the undeniable historical significance Ho Tung Gardens arguably renders its preservation a socially beneficial endeavour,<sup>108</sup> a legal regime that prohibits development without providing compensation<sup>109</sup> imposes the entire cost

<sup>101</sup> *Armstrong v United States*, 364 US 40 (1960); Niemann and Shapiro (n 100 above), p 57; Mark Fenster, 'The Takings Clause, Version 2005: The Legal Process of Constitutional Property Rights' (2007) 9 *U. Pa. J. Const. L.* 667, 694–698.

<sup>102</sup> Stelle Garnett, 'The Neglected Political Economy of Eminent Domain' (2006) 105 *Mich. L. Rev.* 101, 120; Serkin (n 98 above), p 718; Saul Levmore, 'Just Compensation and Just Politics' (1990) 22 *Conn. L. Rev.* 285, 309.

<sup>103</sup> Jonathan H Adler, 'The Adverse Environmental Consequences of Uncompensated Land-Use Controls' in Benson (n 1 above), pp 187, 196; Fenster (n 101 above), pp 699–702; McLaughlin (n 98 above), p 172.

<sup>104</sup> Brown and Stroup (n 1 above), p 224.

<sup>105</sup> Fenster (n 101 above), pp 707–709; Serkin (n 98 above), pp 706–707.

<sup>106</sup> Michael Heller and Rick Hills, 'Land Assembly Districts' (2008) 121 *Harv. L. Rev.* 1465, 1481; Steven J Eagle, 'Property Tests, Due Process Tests and Regulatory Takings Jurisprudence' [2007] *B.Y.U.L. Rev.* 899, 926; Charles E Cohen, 'Eminent Domain After *Kelo v. City of New London*: An Argument for Banning Economic Development Takings' (2006) 29 *Harv. J.L. & Pub. Pol'y* 491, 541–542.

<sup>107</sup> Adler (n 103 above), pp 196–197; Serkin (n 98 above), pp 708–709; Eagle (n 3 above), p 188.

<sup>108</sup> For a discussion of the social value of heritage, see Salla (n 2 above), pp 1–4; Ross (n 1 above), pp 1–9.

<sup>109</sup> The US literature clearly identified the requirement of due process, in particular notice and the right of hearing, given the restrictions imposed on the affected owners' properties, but are more ambiguous as to the constitutional necessity of compensation: Norman Tyler, *Historic Preservation: An Introduction to Its History, Principles, and Practice* 78–81 (W. W. Norton & Company, 2000); Kass, LaBelee and Hansell (n 4 above), pp 198–200 and 209–219.

of the socially beneficial endeavour onto the individual property owner. Although the owner of a large mansion in an exclusive residential district does not present the stereotypical image of an oppressed minority, a growing populist movement in favour of heritage conservation is not always sensitive to the associated costs.<sup>110</sup> In such circumstances, even providing public consultation<sup>111</sup> or other forms of democratic checks<sup>112</sup> are of limited protection to the property owner because the public in general would be broadly supportive of the public goods of historical preservation, but relatively indifferent to the private costs of development restrictions. In the Ho Tung Gardens saga, the erroneous assumption of compensation helped constrain an excessive use of the potentially far-reaching power of monument declaration.

Moreover, this erroneous assumption positively framed the government responses and public discourse surrounding the preservation of Hong Kong's historical heritage. The issue became not simply whether the site is of historical significance and value, but whether it is worth the considerable compensation that the government must pay as compensation for lost development rights. This forces government actors and public commentators to confront the real substantial costs associated with legislative and executive initiatives to preserve historical buildings. This facilitates dialogue and debate beyond the one-sided issue about the efficacy of historical preservation measures and onto the more critical question of the social efficiency of government actions.

### ***B. Perverse Incentives for Property Owners***

Aside from the important constraints on government actors to ensure fairness and efficiency, adequate compensations for regulatory takings is necessary to create incentives for property owners to invest in and manage their property. When confronted with a significant risk of uncompensated regulatory burdens, property owners are likely to underinvest in their property for fear of losing their investment in a government regulatory

<sup>110</sup> For example, Philip Bowring, "Identity Sold for a Quick Profit", *South China Morning Post*, 18 March 2012, p 16 (considering the claims of compensation by owners Ho Tung Gardens as "evidence of greed" and opining that "inheritors of historic buildings are expected to be their guardians"); Michael Chugani, "Public Eye", *South China Morning Post*, 26 October 2011, p 2 ("Other tycoons before her have plundered our heritage for profit").

<sup>111</sup> One example of incorporating public consultation in land administration is the drawing up of zoning plans under the Town Planning Ordinance: Cruden (n 16 above), pp 555–562.

<sup>112</sup> A public consultation on whether the monument declaration for Ho Tung Gardens should proceed was proposed but not carried out eventually: "Weighing the Cost of Saving the Past", *South China Morning Post*, 17 October 2011, p 14.

action.<sup>113</sup> Such risks will also reduce the value of property in general because potential buyers will discount the price of the property by the risk of value-diminishing government regulatory actions,<sup>114</sup> which actually helps constrain the government's decision in Hong Kong. The dominance of land sales and other land-associated revenue as a source of government revenue in Hong Kong<sup>115</sup> results in an unwillingness of the government to adopt measures that might otherwise erode land and property values.<sup>116</sup>

In the particular context of the Ordinance, the primary concern is that inadequate compensation creates a perverse incentive for the property owner that harms the legislative and policy objectives of historical conservation. Without adequate compensation, a monument declaration might impose huge financial losses to the affected property owner. However, as opposed to general regulatory settings, the property owner can unilaterally reduce the risk of the regulatory burden imposed by the Ordinance. Although a property owner can do little to avoid a financially damaging downzoning during a re-zoning exercise,<sup>117</sup> a property owner can avoid having property declared a monument by demolishing or otherwise developing any property that may be considered of historical significance. This risk of pre-emptive destruction was demonstrated during a preservation effort of the King Yin Lei mansion. After a concerted community effort in 2004 successfully pressured the owner to cancel the auction of the mansion,<sup>118</sup> the owner began demolishing the building (unannounced) in 2007 and was only stopped by a proposed monument declaration.<sup>119</sup> Such actions, although logical from the incentive perspective of property owners, severely undermine the legislative objectives of the Ordinance.

The perverse incentive placed on property owners to destroy the things that the legislation intends to protect applies to other forms of regulations that unilaterally impose restrictions on private property.

<sup>113</sup> Serkin (n 98 above), p 715. While the takings literature identifies the risk of over-compensation where market value for the property is claimable, that risk appears to be small when compared to inefficiencies of under-compensation: Adler (n 103 above), p 188.

<sup>114</sup> Brown and Stroup (n 1 above), p 222; Lawrence Blume, "Compensation for Takings: An Economic Analysis" (1984) 72 *Cal. L. Rev.* 569, 584–590.

<sup>115</sup> Lawrence WC Lai, "A Model of Planning by Contract: Integrating Comprehensive State Planning, Freedom of Contract, Public Participation and Fidelity" (2010) 81(6) *The Town Planning Review* 647, 665; CY Jim, "Planning Strategies to Overcome Constraints on Greenspace Provision in Urban Hong Kong" (2002) 73(2) *The Town Planning Review* 127, 146.

<sup>116</sup> Jim (n 115 above), p 146.

<sup>117</sup> Indeed, *Fine Tower Associates Ltd v Town Planning Board* provides an example of cruel irony where the down-zoning was prompted by the application of up-zoning by the affected owners: *Fine Tower Associates Ltd v Town Planning Board* (n 74 above), pp 557–558.

<sup>118</sup> Peggy Sito and Chloe Lai, "Historic House Taken off the Market", *South China Morning Post*, 23 June 2004, p 1.

<sup>119</sup> Martin Wong and Dennis Chong, "Minister Call Times on Wreckers", *South China Morning Post*, 15 September 2007, p 1.

In the context of environmental regulations, various empirical studies in the US have demonstrated that the risks of uncompensated land-use restrictions to protect endangered species and other natural heritages induce pre-emptive destruction of those natural heritages.<sup>120</sup> This confirms the numerous anecdotal accounts in which property owners actively destroyed habitats that were suitable for endangered species for fear of the financially damaging restrictions imposed under the U.S.'s Endangered Species Act.<sup>121</sup>

Of course, there are other property owners who would voluntarily preserve their historical buildings.<sup>122</sup> However, these owners are not the real concern of the Ordinance. Property owners who place economic value over historical preservation have always been the target of historical preservation laws. For example, the impetus of the UK legislative amendment to strengthen the legal powers for historical preservation in 1913 was the Tattershall Castle scandal, which involved an American syndicate of speculators purchasing a five-hundred-year-old castle and selling off individual mantelpieces to art dealers for maximum profit.<sup>123</sup> The perverse incentive to actively destroy or redevelop old buildings under a legal regime that does not award adequate compensation will be particularly strong for such property owners.

### ***C. The (Illogical) Distinction between Money and In-Kind Compensation***

In addition to the unarticulated and unresolved basis of compensation assessment, the Ho Tung Gardens also highlighted a less conspicuous but nevertheless important issue in the Ordinance, ie the checks and balances on the use of public resources in conservation. The approval of the Chief Executive is required whenever compensation is to be paid out to private entities, whether as compensation for financial losses resulting from monument declaration,<sup>124</sup> reimbursement of maintenance, preservation or restoration work on the monument<sup>125</sup> or reward for discovering

<sup>120</sup> Adler (n 103 above), pp 191–194 (discussing the various studies).

<sup>121</sup> *Ibid.*, pp 189–190.

<sup>122</sup> Of the seven private properties that were declared as monuments since 2008, no ostensible compensation in any forms was needed for six of them. The six are Maryknoll Convent School, Residence of Ip Ting Sz, Yan Tun Kong Study Hall at Ping Shan of Yuen Long, Tung Wah Museum, Man Mo Temple on Hollywood Road and Tang Kwong U Ancestral Hall at Kam Tin of Yuen Long: Official Records of Proceedings (Legislative Council of Hong Kong), 23 November 2011, 2335.

<sup>123</sup> Sax (n 73 above), p 1566.

<sup>124</sup> Antiquities and Monuments Ordinance (Cap 53) ss 8 and 9.

<sup>125</sup> *Ibid.*, s 7.



antiquities.<sup>126</sup> In addition, s 21 provides that monetary compensation under the Ordinance is to be paid for by funds provided by the Legislative Council.

This legal regime draws a distinction between compensation paid out in cash and compensation in kind. Only the former is subject to the mandatory legislative oversight of budgetary control. In-kind compensation, whether in the form of land exchange, beneficial re-zoning or relaxation of plot ratios, is not subject to legislative approval because it does not involve payment of public funds. This discrepancy was raised in the legislative debate by the chairman of the subcommittee responsible for the Ho Tung Gardens preservation<sup>127</sup> and elicited a response from the Secretary that, although the Legislative Council does not approve compensation for which there is no payment of cash, other approval bodies are involved for other forms of compensation. For example, re-zoning and increasing plot ratios requires the approval of the Town Planning Board, whereas the relevant District Councils are consulted in the cases of land exchange.<sup>128</sup>

The requirements for obtaining the approval of these other regulatory bodies are of limited value as checks and balances because they are all part of the executive branch. In fact, the negotiation process of the Ho Tung Gardens reveals the wide array of in-kind compensation offered to the property owner, including a land swap of an adjacent site that was zoned as a green belt and redesigning the building plan. There are no suggestions or reports of any intra-bureaucratic standoffs between the different regulatory bodies and the Secretary in her role to preserve Ho Tung Gardens. Indeed, the offering of in-kind compensation is clearly the preferred mode of compensation, at least in the realm of historical preservation. In the earlier high-profile conservation effort of the King Yin Lei mansion, the monument declaration was secured by offering an adjacent site that was originally zoned as a green belt.<sup>129</sup> In the case of Haw Par Mansion, the historic mansion and garden were transferred to the government in exchange for a plot ratio of quantity equal to the floor area of the transferred property.<sup>130</sup>

This discrepancy is not merely legal; it extends to public and political discourse. Statements by government officials reveal an aversion to using public funds to preserve historic buildings and a preference for achieving preservation without spending cash. For example, although the Secretary

<sup>126</sup> *Ibid.*, s 11(4).

<sup>127</sup> Official Records of Proceedings (Legislative Council of Hong Kong), 16 March 2011, 7962–7965.

<sup>128</sup> *Ibid.*, p 7973.

<sup>129</sup> Lung (n 16 above), p 137; Ng (n 41 above); Cruden (n 16 above), p 39.

<sup>130</sup> Lung (n 16 above), p 136.

did correctly observe that “public resources will be committed” whenever public money or land exchange is utilised for compensation,<sup>131</sup> she nevertheless took pains to emphasise during the legislative debate that “[n]o public money was involved” in resolving a prior preservation effort of King Yin Lei.<sup>132</sup> This was echoed by her earlier statements against the use of “hard cash” to purchase historical buildings in private ownership.<sup>133</sup> Indeed, she observed that other countries “seldom opted for spending public money on compensation to undertake heritage preservation”.<sup>134</sup> Similarly, although local academic David Lung recognised that the government was in fact “buying back” ownership of the historic properties for conservation efforts, he also considered it significant that public revenue was not spent.<sup>135</sup>

However, there is no distinction between monetary compensation and in-kind compensation from the incentive perspective. Both are economically valuable to the recipients and economically costly to the providers. The economic value to the recipients is obvious; otherwise, property owners affected by monument declaration would not have agreed to forgo profitable development. The recipients of in-kind compensation that involves the transfer of physical property (such as a land exchange) can easily cash out the monetary value of these in-kind compensations. A similar principle applies to upzoning, which is the relaxation of plot ratios and other beneficial regulatory actions offered as compensation. There is again no fundamental distinction between “property” and “regulation” in terms of the financial impact on recipients,<sup>136</sup> and it is not uncommon for the enhancement of property values that arises from favourable planning/zoning decisions to dwarf the entire value of the land prior to such decision.<sup>137</sup>

In-kind compensation is also costly to the provider even if there is no ostensible payment of monies. At first glance, an in-kind compensation that involves a land exchange, such as a green belt, seems to successfully

<sup>131</sup> Official Records of Proceedings (Legislative Council of Hong Kong), 16 March 2011, 7972.

<sup>132</sup> Official Records of Proceedings (Legislative Council of Hong Kong), 23 November 2011, 2335.

<sup>133</sup> Official Records of Proceedings (Legislative Council of Hong Kong), 9 November 2011, 1742–1743.

<sup>134</sup> Official Records of Proceedings (Legislative Council of Hong Kong), 16 March 2011, 7973.

<sup>135</sup> Lung (n 16 above), p 137 (“The public was willing to give up a piece of green belt land in exchange for a historic complex without spending public revenue. This example can be considered as the first of its kind success achieved in protecting historic buildings in private ownership”).

<sup>136</sup> Eagle (n 3 above), p 332.

<sup>137</sup> Tom Allen, “Controls over the Use and Abuse of Eminent Domain in England: A Comparative View” in Robin Paul Malloy (ed), *Private Property, Community Development, and Eminent Domain* (Ashgate, 2008) 75, 95 (£7000 per hectare mixed use agricultural land versus £ 2.6 million per hectare of residential “bulk” land).

secure historical preservation without any real public expenditure. However, this in-kind compensation decreases public assets (in this case, the valuable resource of land in land-scarce Hong Kong). In addition, the public coffers will suffer even more if the revenue that could be derived from the public auction of that land is larger than the legally payable compensation.

This critique applies with identical force to beneficial regulatory actions that do not involve the transfer of any physical property to the recipients. Given the real economic benefits of the beneficial regulations to the recipients, it is not surprising that they can be monetised by the government. In Hong Kong, there is an established practice of collecting a premium for lease modifications designed to take advantage of an upzoning of the area.<sup>138</sup> This practice allows the government to recoup the enhancement of economic value arising from the change in zoning. Thus, using beneficial regulations as a form of in-kind compensation involves real opportunity costs of monetising those regulations. Moreover, regulatory actions often inevitably affect the community at large. When regulatory actions are meant to serve as compensation to private owners, the public as a whole suffers from this departure from the original purpose of these regulations. For example, land originally zoned as green belt is commonly offered in a land exchange to secure monument declaration. The necessary change in zoning reduces the available greenery and other important environmental benefits of green-belt zoning.<sup>139</sup>

Hence, the dichotomy between monetary compensation and in-kind compensation that shapes the disparity in checks and balances under the legal regime and permeates the public and political discourse is an artificial dichotomy. This can give rise to inefficiencies and injustices from overcompensation. Although the inclusion of the potential hefty compensation in the public discourse about historical preservation is integral to achieving a socially efficient outcome, the lack of emphasis paid to non-monetary compensation creates perverse incentives for the government to offer excessively in-kind compensation (whether in the form of land exchange or beneficial land-use regulatory changes) to secure the property owner's consent to monument declaration. With such overcompensation, the government avoids the owner's claim for monetary compensation while relieving itself of the potential political backlash from a failing historical conservation programme. The property

<sup>138</sup> Lai (n 115 above), p 665; Roger Nissim, *Land Administration and Practice in Hong Kong* (Hong Kong University Press, 2nd ed, 2008) 69–75.

<sup>139</sup> Jim (n 115 above), p 128.

owner is also more likely to accept this generous in-kind compensation. However, the public coffers and the public at large suffer whenever such overcompensation is paid out.

Conversely, there is the risk of undercompensation whenever monetary compensation is payable, as arguably demonstrated by the example of Ho Tung Gardens. Although the government clearly recognised the historical value of Ho Tung Gardens, the monument declaration was derailed simply because of the aversion to paying cash. What is tellingly unfortunate is that this result was not caused by a lack of economic resources or lack of commitment to utilise those resources for compensation; on the contrary, the government is willing to offer substantial in-kind compensation (such as exchanging land of equal value) to secure historical preservation. The fact that the affected owner is not interested in such in-kind compensation should not, in theory, be an obstacle because the government can simply monetise the in-kind compensation (eg auction off the land that is proposed for land exchange) to pay the owner in cash. However, there is strong incentive in the executive branch to avoid this course of action because, once monetised, the revenue is subject to legislative approval (and greater public scrutiny),<sup>140</sup> whereas the use of land (including for exchange) or regulatory actions is entirely within the domain of the executive branch.<sup>141</sup>

#### ***D. Fiscal Pressure***

Imposing the fiscal burden onto the government forces it to confront the economic consequences of its actions, but the approach is not without problems. For instance, conservation efforts are likely to be derailed in times of economic constraints.<sup>142</sup> This is particularly so within the context of Hong Kong, which is required under the Basic Law to maintain low-tax policies and limited fiscal deficit.<sup>143</sup> The requirement of substantial compensation may compel the government to underperform in its conservation efforts. The government may avoid making a monument declaration unless it is completely certain of the historical significance of a monument. This is not necessarily a problem in other regulatory settings because the government should always be careful not

<sup>140</sup> Richard Cullen *et al.*, "Fiscal Policy and Financial System" in Chan and Lim (n 14 above), pp 321, 326–328 (discussing the Legislative Council role in budget and fiscal control).

<sup>141</sup> Nissim (n 138 above), pp 55–68 (discussing the functions and powers of the Lands Department – the government executive department responsible for land administration).

<sup>142</sup> Halfin (n 71 above), p 15 (criticizing the UK experience).

<sup>143</sup> Cullen (n 140 above), p 340.

to unduly burden private property rights. Moreover, the government can always reverse course at a later date with better evidence of the need of regulatory intervention. However, the particular problem with historical conservation is that there is no opportunity to reverse course once the property is demolished and/or redeveloped.

The problem of fiscal pressure is further aggravated by the fact that heritage conservation is considered in the economics literature as a luxury and positional good – demand for this type of good increases as wealth grows.<sup>144</sup> Thus, a dwindling of the state coffers (perhaps because of a financial downturn) will both increase the tension between historical preservation and other government expenditures and decrease the public demand for historical preservation in relation to other policy matters.

## V. What the Law Should Be

The analysis from the incentive perspective in the previous section highlights the imperative for reform in Hong Kong. This part outlines a set of reform guidelines by drawing from the parallel experience in the UK. The UK legal regime provides a useful comparative case study for two reasons. First, although the UK legal regime was not expressly mentioned during the legislative debate in Hong Kong, the Ordinance broadly resembles the framework of the flagship legislation on historical preservation in the UK – the Ancient Monuments and Archaeological Areas Act 1979.<sup>145</sup> This is not surprising because Hong Kong was a British colony when the Ordinance was enacted and continues to be strongly influenced by the English common law.<sup>146</sup> Second, the relevant UK legal regime has been in force for a much greater period of time, with several legislative reforms and developed case law since its inception in the late nineteenth century. Any reform proposals in Hong Kong should learn from the UK experience to avoid similar pitfalls.

### A. Comparative Perspective: the U.K.

#### 1. General legal framework

There are two primary legal tools for historical preservation in the UK. The first, the Ancient Monuments and Archaeological Areas Act, was enacted

<sup>144</sup> Brown and Stroup (n 1 above), pp 211–212.

<sup>145</sup> Chapter 46 (1979) (UK).

<sup>146</sup> Johannes Chan, “The Judiciary” in Chan and Lim (n 14 above), p 289.

in 1979<sup>147</sup> to consolidate existing laws, such as the Historic Buildings and Ancient Monuments Act of 1953<sup>148</sup> and the Town and Country Planning (Amendment) Act of 1972.<sup>149</sup> The Ancient Monuments and Archaeological Areas Act is the most relevant legal tool for our inquiry because, similar to its Hong Kong counterpart, the preservation of historical buildings under this legislation is achieved through the scheduling (ie declaration) of monuments.<sup>150</sup> A “scheduled monument consent” from the responsible regulatory authority (ie the Secretary of State) is required for any alteration or demolition work proposed to be undertaken on a scheduled monument,<sup>151</sup> with compensation payable for refusal.<sup>152</sup>

The other relevant legislation is the Planning (Listed Buildings and Conservation Areas) Act 1990<sup>153</sup>, which maintains a schedule of “listed buildings”. The designation of a “listed building” imposes a duty on the relevant planning authorities to consider the architectural or historic interests of the “listed building” during the determination of planning permissions.<sup>154</sup> A listed building consent is also required from the relevant local planning authorities for any work undertaken on the premises.<sup>155</sup> The difference between a “listed building” and a “scheduled monument” is mainly one of degree. Reflecting the lower threshold of historical significance that will trigger a “listing” compared to a “scheduling”, the legal protection afforded to a “listed building” is less than that of a “scheduled monument”.<sup>156</sup> The mere act of listing does not trigger a statutory presumption in favour of preservation, and it is up to the local planning authorities in their exercise of their planning function<sup>157</sup> to

<sup>147</sup> For a discussion of the UK historical conservation law from the historical perspective, see generally Sax (n 73 above). For a discussion of the framework of the Ancient Monuments and Archaeological Areas Act 1979, see Halfin (n 71 above), pp 10–13. For a discussion about overall historic preservation regime in UK, see Salla (n 2 above), pp 111–139.

<sup>148</sup> Chapter 49 (1953) (UK).

<sup>149</sup> Chapter 42 (1972) (U.K.).

<sup>150</sup> Ancient Monuments and Archaeological Areas Act 1979 (Ch 46) s 1.

<sup>151</sup> *Ibid.*, s 2.

<sup>152</sup> *Ibid.*, ss 7–8.

<sup>153</sup> Chapter 9 (1990) (UK).

<sup>154</sup> Planning (Listed Buildings and Conservation Areas) Act 1990 (Ch 9) s 66.

<sup>155</sup> *Ibid.*, ss 7–8.

<sup>156</sup> For a discussion of the consequences of listing, see Salla (n 2 above), pp 123–127; Roger W Suddards *et al.*, *Listed Buildings: The Law and Practice of Historic Buildings, Ancient Monuments, and Conservation Areas* (Sweet & Maxwell, 3rd ed, 1996) 58–64; Mnynors (n 92 above), pp 47–50.

<sup>157</sup> This planning function involves the balancing of various social and economic factors associated with the planning of the entire function, with heritage conservation merely a factor of consideration, albeit an important one nonetheless: Suddards (n 156 above), pp 106–180 (discussing the criteria for listed building consent).

decide whether a listed building consent will be issued.<sup>158</sup> The financial impact of “listing” is also more ambivalent,<sup>159</sup> and no compensation is provided for the refusal of planning permissions.<sup>160</sup>

## 2. *The compensation provision*

Section 7 of the Ancient Monuments and Archaeological Areas Act contains the right of compensation for “loss or damage” arising from “the refusal, or the granting subject to conditions, of a scheduled monument consent”. Section 7 expressly sets forth in some detail the different calculations of compensation in the various scenarios. In particular, s 7(6) provides that loss or damage includes “depreciation of the value of an interest in land”, calculated under the assumption that any refusal or conditions imposed would continue to be imposed for any subsequent applications for works of a similar nature. This is an important clarification about the basis of compensation because it resolves the ambiguity of whether the court must assess and take into account the likelihood of the refusal (or conditions imposed) being lifted in the future. Conversely, s 7(4) provides that there is no compensation if the work involves total or partial demolition of the monument<sup>161</sup> and if the planning permission (other than by a general development order)<sup>162</sup> for the demolition work had not been granted before the monument was scheduled as a monument.<sup>163</sup>

A notable feature of the UK legislation is the provision of compensation recovery in the event of the reversal of the refusal to grant consent for development work on the scheduled monument.<sup>164</sup> This serves to balance the otherwise generous assumption under s 7(6) that future application for consent to undertake the development work would be refused. The owner of the scheduled monument would not be undeservingly enriched if the owner claimed compensation for refusal but then subsequently managed to obtain consent, perhaps because of a change in government or conservation policy.

<sup>158</sup> Mynors (n 92 above), p 47.

<sup>159</sup> *Ibid.*, p 50 (“In other cases listing may be advantageous, as is shown by the number of estate agents’ particulars which make a feature of it”).

<sup>160</sup> Planning (Listed Buildings and Conservation Areas) Act 1990 (Ch 9) s 27; Mynors (n 92 above), p 250. There is a right to force the local authority to purchase the property in the narrow grounds that there is no longer any reasonable beneficial uses because of the refusal of permission: Suddards (n 156 above), pp 200–202; Mynors (n 92 above), pp 252–254. However, this right merely reflects well-established doctrine of regulatory takings – compensation is only payable where all economic use/value is destroyed by the regulation: above Part III.C.

<sup>161</sup> Ancient Monuments and Archaeological Areas Act 1979 (Ch 46) s 7(4).

<sup>162</sup> A general development order is “a development order made as a general order applicable (subject to such exceptions as may be specified therein) to all land”: *ibid.*, s 7(7).

<sup>163</sup> Ancient Monuments and Archaeological Areas Act 1979 (Ch 46), s 7(2)(a).

<sup>164</sup> *Ibid.*, s 8.



### 3. Application

In the only case that assessed the compensation provision of the 1979 act,<sup>165</sup> the Scottish Lands Tribunal in *Currie's Executors v Secretary of State for Scotland*<sup>166</sup> set the date of assessment for loss as the date of the refusal of the consent. More significantly, any losses in property value caused by policy changes after the monument declaration but prior to the date of refusal are not claimable.<sup>167</sup> This is the case even if the policy changes – although effected independently by a different regulatory department – were made with the intention to protect scheduled monuments.<sup>168</sup> This decision echoed the earlier decision of *Hoveringham Gravels Ltd v Secretary of State for the Environment*,<sup>169</sup> which applied the more simplified compensation provision (s 12) of the predecessor legislation, the Historic Buildings and Ancient Monuments Act of 1953. The court in *Hoveringham Gravels Ltd v Secretary of State for the Environment* found that no compensation is payable because planning permissions under the Town and Country Planning Act of 1971 would not be granted for the proposed development that is also the subject matter of the scheduled consent. This is the case even if the refusal of planning permission is related to possible harm to an ancient monument.<sup>170</sup>

Although the assessment of compensation is not frequently litigated, the compensation payable for scheduling a monument remains an integral part of the government's decision-making process. One high-profile event under this scheme was the discovery of the Shakespearean Rose Theatre in 1989. Notwithstanding the recognised national importance of the site, the Secretary of State (the relevant government authority for monument scheduling) decided against scheduling. One of the explicit reasons proffered was the risk of substantial compensation that would become payable to the developer because a planning permission had previously been granted for development of the site.<sup>171</sup>

<sup>165</sup> Michael Ross opined that the claims in compensation only arise "[i]n certain rather unusual circumstances": Ross (n 1 above), p 149.

<sup>166</sup> 1992 SLT (Lands Tr) 69.

<sup>167</sup> *Ibid.*, p 72.

<sup>168</sup> In *Currie's Executors v Secretary of State for Scotland*, no compensation was awarded because the value of the intended use by the owner (forestry) had already been severely reduced when the Forestry Commission decided to stop giving forestry grants to reforestation efforts on ancient monuments. For a critical analysis of this decision, see Jeremy Rowan-Robinson, "Compensation for Safeguarding Archaeological Remains" (1992) 37 *Scottish Planning Law & Practice* 81.

<sup>169</sup> [1975] QB 754.

<sup>170</sup> *Ibid.*, p 764–762. For a discussion of the case, see Cruden (n 16 above), p 42; Suddards (n 156 above), pp 301–302.

<sup>171</sup> A judicial review was brought against the government decision, but was dismissed on account of the wide discretion afforded to the Secretary of State under the statute. The monument was nevertheless scheduled in 1992. For an account of the incident, see Suddards (n 156 above), pp 303–304.

## ***B. Reform Guidelines***

The discussion above highlights three important considerations that should inform a well-designed compensation scheme for historical preservation.

### *1. Adequacy of compensation*

Adequate compensation is important because it ensures that a more comprehensive and accurate assessment of the costs of historical preservation is taken into account during the processes of public debate and government decision making. Moreover, adequate compensation mitigates the perverse incentives of property owners to destroy the historical significance of their property before far-reaching restrictions of monument declaration are placed on it.

Of course, the adequacy of such compensation is subject to intense controversies. The UK legislation focuses on the depreciation in land value caused by restrictions on development.<sup>172</sup> A similar basis is adopted in Hong Kong for the development restrictions imposed during the construction of the Mass Transit Railway or for nature preservation.<sup>173</sup> Notwithstanding the inevitable debate as to the appropriate valuation method,<sup>174</sup> compensation for the depreciation in land value is conceptually sound because it captures the objective economic losses suffered by the property owner. Moreover, although awarding fair market value in eminent domain cases has not prevented criticisms of undercompensation,<sup>175</sup> many of these critiques are not applicable to the restrictions associated with monument declaration. For example, sentimental attachment to a property that may result in the subjective value of the property being higher than fair market value<sup>176</sup> will not be destroyed under the monument declaration (in fact, it will be better protected). Similarly, monument declaration will only generate limited relocation and replacement costs – significant costs that are not reflected in fair market value<sup>177</sup> – because property owners remain entitled to live and use the premises without disturbance.

<sup>172</sup> See above Part V.A.

<sup>173</sup> See above Part III.A.

<sup>174</sup> See Cruden (n 16 above), pp 593–629 (discussing the various valuation methods utilized in Hong Kong for land administration cases). See generally Wallace Kaufman, “How Fair is Market Value?” in Benson (n 1 above), p 77 (discussing the various potential distortions in the valuation process that may result in either under or over compensation).

<sup>175</sup> James J Kelly, Jr., “‘We Shall Not be Moved’: Urban Communities, Eminent Domain and the Socioeconomics of Just Compensation” (2006) 80 *St. John’s L. Rev.* 923, 940; Eagle (n 3 above), pp 189–190.

<sup>176</sup> Garnett (n 102 above), p 107; Eagle (n 106 above), p 926.

<sup>177</sup> Garnett (n 102 above), p 106; Cohen (n 106 above), p 538.

There is a shortcoming in the current UK regime that must be remedied to avoid undercompensation. The otherwise adequate compensation provided for in the Ancient Monuments and Archaeological Areas Act is subject to two important qualifications. First, a prior planning permission must be in place before compensation for refusal of scheduled consent may be claimed. This requirement is likely to induce a property owner to ensure that a planning permission for maximum development is in place for the property at all times to safeguard the right of compensation. Applying for planning permission is a waste of private and public resources when it is made for the purpose of compensation rather than for genuine development.

More problematic is the second qualification, in which the reduction in land value caused by other regulatory schemes would be excluded from compensation even if the regulatory burdens were advanced for purposes of heritage conservation. Historical value will effectively continue to increase the risk of financially disastrous regulatory burdens that would not be compensated. Adequacy of compensation must ensure that governmental authority cannot circumvent the compensation provision by utilising other legislative or regulatory schemes that do not provide for compensation.<sup>178</sup> This is not a problem for building permission in Hong Kong because the assessment by the Building Department is restricted to structural safety issues and compliance with zoning plans.<sup>179</sup> However, it is a problem regarding zoning under Town Planning Ordinance (Cap 131) because the regulatory mandate is broadly worded to include the “promotion of the health, safety, convenience and general welfare of the community”.<sup>180</sup> Indeed, there is judicial recognition that the Town Planning Board can take into account the presence of historical sites in formulating development restrictions and other zoning matters.<sup>181</sup> As no compensation is payable for downzoning,<sup>182</sup> there is a possibility that the government will game the system by first downzoning the property before a monument declaration. To preserve adequacy of compensation as a safeguard against pre-emptive destruction, it will be important to include financial losses that arise from other regulatory actions motivated by heritage conservation.

<sup>178</sup> Cf. *Westminster Bank Ltd v Beverley Borough Council* [1971] AC 508 (HL) (holding that when there are two alternative courses open to a public authority – one of which gives rise to compensation and the other does not – the authority is entitled to adopt the one which does not give rise to compensation)

<sup>179</sup> Buildings Ordinance (Cap 123) s 16. For a discussion of the relevant case law, see Cruden (n 16 above), pp 48–54.

<sup>180</sup> Town Planning Ordinance (Cap 131) s 3.

<sup>181</sup> *Oriental Generation Ltd v Town Planning Board* (n 84 above), [7] (they include one grade 1 listed building and a grade 3 listed building).

<sup>182</sup> See above Part III.C.

In any event, the basis of the compensation should be clearly delineated to ensure transparency. Although the erroneous assumption of hefty compensation in the Ho Tung Gardens saga promoted the proper framing of the issue in public discourse, the lack of an expressly articulated method of compensation assumption resulted in a wide range of compensation amounts being bandied about. Moreover, these figures are often incorrect even if the legal basis were deemed to be the diminution of property value. As noted above, the substantial construction costs and the value of the existing property should be deducted from the HK\$3 billion price tag of the redevelopment. This renders the headline in the local English press – “Taxpayers Face HK\$3b Bill for Mansion” – arguably misleading.<sup>183</sup> Indeed, the compensation figure in the press report was raised to HK\$7 billion simply after the owner declared it.<sup>184</sup> This ambiguity was not clarified in any way by the public stance of the government that purportedly did not undertake an assessment of the monetary compensation payable.<sup>185</sup> Certainty in assessing compensation will ensure that neither the public discourse nor the government decision-making process is distorted by either overcompensation or undercompensation.

## *2. No distinction between in-kind compensation and monetary compensation*

The compensation scheme should avoid making the distinction between in-kind compensation and monetary compensation. The fact that in-kind compensation does not necessarily involve an explicit expenditure of public funds neither reduces the need for checks and balances nor the consideration of public finances. In particular, the in-kind compensations typically used by the Hong Kong government as “economic incentives” for historical preservation are all capable of monetary quantification.

This does not imply that in-kind compensation should be prohibited. There are circumstances in which in-kind compensation is more efficient. For example, if compensation can only be paid in monetary terms, transaction costs must be incurred to monetise the in-kind compensation (eg public auction to sell the land used for land exchange) before transfer to the affected property owners. Insofar as such monetisation would not have occurred but for the compensation payable under the monument declaration, these transaction costs are additional deadweight costs

<sup>183</sup> Ng (n 47 above).

<sup>184</sup> Joyce Ng, “Preservation More Than a Matter of Trust”, *South China Morning Post*, 22 January 2012, p 4.

<sup>185</sup> Official Records of Proceedings (Legislative Council of Hong Kong), 23 November 2011, 2334–2335. No reason was offered for the failure to undertake the assessment, despite the real likelihood that negotiation would not succeed given the refusal of the previous offers of in-kind

that benefit neither the government nor the property owners. In-kind compensation may also be of particular value to the affected property owner. There may be some particular subjective preference regarding the location of the premise that would not be captured by a general assessment of the market value of the property.<sup>186</sup> A land exchange involving property from an adjacent site might be particularly valuable to the owner without increasing the burden on the government. Similarly, the relaxation of plot ratios and other beneficial zoning may provide special value to a particular development project undertaken by the affected owners, perhaps because of a unique architectural or development concept, that will not be reflected if “sold” to other property owners. There is no reason to bind the government’s compensation options in such circumstances. This article simply argues that similar approval mechanisms should be adopted for both in-kind and monetary compensation.

### 3. *Regular financial commitment*

Given that historical preservation is not a public benefit that can be readily quantifiable<sup>187</sup> and is a positional good that responds adversely to a reduction in spending power,<sup>188</sup> a robust historical preservation compensation scheme must be resistant to cyclic fiscal pressure. The current practice of seeking approval for legislative funding in an ad hoc manner is not desirable. A regular financial commitment to a fund for historical preservation is necessary to ensure that the long term goal is not derailed by short-term fluctuations of either public finance or political will.<sup>189</sup> In this regard, the UK regime that allows the government to claw back the compensation paid out in the event that the government reverses its decision on preservation (eg if a later assessment finds that development should be allowed at the monument) helps mitigate the problem to a certain extent by reducing the fiscal costs of any mistaken monument declaration. However, because this rule only provides a fiscal benefit in the future, there is limited impact on the incentives of the current government in light of possible changes in the ruling party. Thus, a regular commitment to a fund designated for historical preservation would be preferable.

compensation. A conjecture is that the government side-stepped the issue to avoid setting an excessively high compensation precedent that may impede future conservation efforts.

<sup>186</sup> Kelly (n 175 above), p 952.

<sup>187</sup> Brown and Stroup (n 1 above), pp 230–231.

<sup>188</sup> See above Part IV.D.

<sup>189</sup> See Baohui Zhang, “Political Paralysis of the Basic Law Regime and the Politics of Institutional Reform in Hong Kong” (2009) 49(2) *Asian Survey* 312, 315–318 and 320–321 (discussing the political paralysis that impedes effective policy initiatives).

## VI. Conclusion

The Ho Tung Gardens saga highlights the considerations that are relevant to a well-designed compensation regime for historical preservation. The positive shaping of public discourse by the normatively desirable but legally flawed assumption of significant compensation underscores the importance of adequate compensation to constrain the government decision-making process and to create proper private incentives for historical conservation. However, the Ho Tung Gardens saga revealed the risks of fiscal pressure and the incoherency of the distinction between in-kind and monetary compensation when the conservation effort was ultimately thwarted by the potential expenditure of significant amounts of public funds for compensation.

Legislative reform is imperative. The compensation provision of the Ordinance should clearly stipulate the basis of compensation as the reduction in the value of the property caused by the development restrictions of monument declaration. This may be achieved by importing the language from compensation provisions in either the UK Ancient Monuments and Archaeological Areas Act or Hong Kong's Country Parks Ordinance, although care must be taken to ensure that compensation includes the reduction in land value arising from other regulatory actions that are motivated by heritage conservation. In addition, there should be no differences in procedures for payment of in-kind compensation and monetary compensation. Finally, a regular financial commitment should be made to historical preservation. These reforms will help ensure that the Ordinance properly advance the goals of historical preservation in an environment of ever-increasing fiscal and development pressures.

On a broader level, the Ho Tung Gardens saga is an illustrative case study of how the incentive perspective may illuminate inquiry into regulatory takings. The design of any regulatory scheme must account for the incentives and abilities of the affected private entities to avoid financially damaging regulatory burdens. In particular, the provision of adequate compensation is critical for regulatory schemes in which targeted private entities can reduce the risk of regulatory burdens by simply destroying the very object the regulatory scheme intends to protect. Regulators should not underestimate the initiative of property owners to advance their interests under any regulatory regime.